

Testator	=
Date 1	=
Date 2	=
Date 3	=
Son	=
Daughter	=
Trust A	=
Trustee	=
State 1	=
Date 4	=
State 2	=
Statute 1	=
Date 5	=
Year	=
Spouse	=
Trust B	=
<u>a</u>	=
Statute 2	=
Statute 3	=
Date 6	=
<u>b</u>	=

Dear \_\_\_\_\_ :

This letter responds to your authorized representative's letter of June 26, 2014, regarding the generation-skipping transfer (GST) tax consequences of a proposed merger of Trust A and Trust B.

### FACTS

The facts and representations submitted are as follows.

Testator executed a will, dated Date 1, and two codicils, dated Date 1 and Date 2. Testator died on Date 3, a date prior to September 25, 1985, survived by Testator's children, Son and Daughter.

Article VII of Testator's will created a trust, Trust A, for the benefit of Son and Son's lineal descendants. The current trustee of Trust A is Trustee. An identical trust was created for Daughter. This private letter ruling pertains to Trust A.

Currently, Article VII, Section 1(2)(iii), provides that the trustee of Trust A shall pay to Son or apply for his benefit the net income in convenient monthly or quarterly installments until the death of Son. Article VII, Section 2 provides that if, in the sole judgment of the trustee, the net income from Trust A, supplemented by funds available from other sources to Son, is not sufficient to meet the reasonable needs of Son in his station in life, then the trustee may pay to or apply for the benefit of Son so much of the principal of Trust A as the trustee in its sole discretion shall from time to time deem requisite or desirable without being required to adjust or account with respect to the interest of any other beneficiary under the provisions of Article VII.

Article VII, Section 1(2)(iv) provides that upon the death of Son, all the funds and properties constituting Trust A is to vest in and be delivered and conveyed to Son's surviving issue, *per stirpes*. If Son leaves no issue surviving him, the assets of Trust A will be added to a trust for the benefit of Daughter. Article VII, Section 4 provides that if Son dies and is not survived by any lineal descendants, by Daughter, or by any lineal descendants of Daughter, the assets of Trust A are to be distributed to the persons who are entitled to take Testator's personal property under the laws of intestacy then in effect in State 1.

Section 3 of Article VII provides that if any of the properties constituting a part of Trust A shall vest in the issue of Son who is under age 21, then such beneficiary's share is to remain in trust until the beneficiary's 21<sup>st</sup> birthday. The trustee may make income or principal distributions to such beneficiary in its sole discretion, for the suitable support

and education of the beneficiary until the beneficiary attains age 21, or sooner die, whereupon the principal and any accumulated income of such trust shall be delivered, discharged of the trust.

On Date 4, upon the appointment of Trustee as successor trustee, the principal place of administration of Trust A was moved from State 1 to State 2 with the consent of Son and Son's living issue, in accordance with Statute 1. Accordingly, Trust A is governed under the laws of State 2.

On Date 5, in Year 1, Son's spouse, Spouse, established an irrevocable trust, Trust B, for the benefit of Son and Son's lineal descendants. The trustee of Trust B is Trustee. Spouse funded Trust B with \$a. Spouse intends to allocate \$a of her available GST tax exemption to the transfer on Spouse's Year Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return. Accordingly, it is represented that Trust B will have an inclusion ratio of zero with respect to the assets contributed by Spouse.

During Son's lifetime, the dispositive terms of Trust B are identical to the provisions of Trust A. Article IV(A) of Trust B provides that the net income of Trust B shall be paid to or applied for the benefit of Son in convenient monthly or quarterly installments until the death of Son. Article IV(B) provides that if, in the sole judgment of the trustee, the net income from Trust B, supplemented by funds available from other sources to Son, shall not be sufficient to meet the reasonable needs of Son in his station in life, then the trustee may pay to or apply for the benefit of Son so much of the principal of Trust B as the trustee in its sole discretion shall from time to time deem requisite or desirable without being required to adjust or account with respect to the interest of any other beneficiary.

Article IV(C) provides that upon Son's death, all the funds and properties constituting Trust B is to be apportioned among Son's surviving issue, *per stirpes*, and each share so apportioned will be held as a separate trust for the benefit of such issue in accordance with Article V of Trust B (Further Trusts). If Son dies leaving no issue surviving, all the funds and properties constituting Trust B shall be delivered outright and free of trust to Daughter, if she is living. If Daughter is not then living, then Trust B shall be delivered outright and free of trust to the surviving issue of Daughter, *per stirpes*. If Son is not survived by living issue, by Daughter, or by any living issue of Daughter, then Trust B shall be delivered outright and free of trust to the then living person or persons who would be entitled to receive the personal property of Testator under the laws of intestacy then in effect in State 1.

Article V provides that the trustee shall hold Trust B in separate trusts for each descendant of Son. Each descendent is referred to as "Beneficiary" for purposes of Articles V. Article V(A) provides that the trustee may pay or apply all or any portion of the net income for the Beneficiary of a Further Trust, in the trustee's absolute discretion. Any net income not paid shall be added to principal. During any taxable year of the

trust in which the net income is less than b percent of the net fair market value of the trust assets as of the first day of such taxable year, trust income shall be deemed to be increased by an amount that, when added to the actual net income of the trust, will equal b percent of the net fair market value of the trust assets as of the first day of such taxable year. Article V(B) provides that the trustee may transfer and pay over all or any part of the principal of the Further Trust to or for the benefit of the Beneficiary.

Article V(C) provides that each Beneficiary shall have the power to appoint, by specific reference to this general power of appointment in the Beneficiary's will, all or any part of the principal and income of the Beneficiary's Further Trust remaining at the time of the Beneficiary's death to one or more lineal descendants of Son, or to the Beneficiary's estate, in such proportions and amounts as the Beneficiary shall designate in the Beneficiary's absolute discretion.

Article V(D) provides that if the Beneficiary does not exercise his or her general power of appointment, the property remaining in the Beneficiary's Further Trust will be apportioned in equal shares with one share for each of the Beneficiary's children who is then living, and one share for each of the Beneficiary's children who is then deceased and survived by living issue, *per stirpes*. If the Beneficiary has no living lineal descendants, the property remaining in the Beneficiary's Further Trust will be apportioned among the Beneficiary's living siblings and the living descendants of any of the Beneficiary's deceased siblings, *per stirpes*. In default of all the foregoing beneficiaries, the property remaining in the Beneficiary's Further Trust will be apportioned among the lineal descendants of Son, *per stirpes*. Each share apportioned for a lineal descendant will be held in a separate trust for that descendant, which will be administered under the terms of Article V of Trust B.

Subject to the receipt of a favorable private letter ruling, Trustee will merge Trust A into Trust B, as reflected in the Trust Merger Agreement dated Date 6. All of the presumptive remainder beneficiaries have consented to the merger of Trust A into Trust B. Following the merger, all of the assets of Trust A and Trust B will be administered in accordance with the terms of Trust B.

Statute 2 provides that a trustee may merge any 2 or more trusts, whether or not created by the same trustor, to be held and administered as a single trust if such a merger would not result in a material change in the beneficial interests of the trust beneficiaries, or any of them, in the trust. A trustee may merge trusts under Statute 2 without authorization by the court. Statute 3.

You have requested the following rulings:

1. The merger of Trust A into Trust B will not cause the portion of Trust A merged into Trust B to lose its status as a "grandfathered" trust exempt from GST tax under § 26.2601-1(b).

2. Future distributions from Trust B attributable to assets received from Trust A to Son or Beneficiary (as defined in Trust B) will not be subject to GST tax.
3. Following the merger of Trust A into Trust B, the portion of the merged trust attributable to the assets received from Trust A and the portion of the merged trust attributable to the assets contributed to Trust B by Spouse will be treated as separate trusts for GST tax purposes.

## LAW AND ANALYSIS

### Ruling 1

Section 2601 of the Internal Revenue Code imposes a tax on every generation-skipping transfer. Section 2611(a) provides that the term “generation-skipping transfer” means: (1) a taxable distribution; (2) a taxable termination; and (3) a direct skip.

Under section 1433 of the Tax Reform Act of 1986 (the Act), the GST tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under § 1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the tax does not apply to a transfer under a trust that was irrevocable on September 25, 1985, except to the extent the transfer is made out of corpus added to the trust by an actual or constructive addition after September 25, 1985.

Section 26.2601-1(b)(1)(ii)(A) provides that any trust in existence on September 25, 1985 will be considered an irrevocable trust except as provided in § 26.2601-1(b)(1)(ii)(B) or (C) (relating to property includible in the grantor’s gross estate under §§ 2038 and 2042).

Section 26.2601-1(b)(4)(i) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the generation-skipping transfer tax under § 26.2601-1(b) will not cause the trust to lose its exempt status. These rules are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. The rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13 if the modification does not shift a beneficial interest in the trust

to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. A modification of an exempt trust will result in a shift in a beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a generation-skipping transfer or the creation of a new generation-skipping transfer.

In the instant case, the merger of Trust A and Trust B is permitted under State 2 law if such merger would not result in a material change in the beneficial interests of the trust beneficiaries. Statute 2. Statute 3 provides that a trustee may act under Statute 2 without the authorization by the court. The beneficiaries, including the presumptive remainder beneficiaries, have consented to the merger of Trust A into Trust B and Trustee executed the Trust Merger Agreement. During Son's lifetime, the terms of Trust A and Trust B are identical. Pursuant to the terms of Trust A, upon Son's death, the assets of Trust A will be distributed outright to Son's surviving issue, *per stirpes*. Pursuant to the terms of Trust B, upon Son's death, the properties constituting Trust B will be apportioned for the benefit of each surviving issue of Son, *per stirpes*, in respective Further Trusts. However, each Beneficiary of a Further Trust is granted a general power of appointment over his or her respective trust, which will cause that trust to be includible in such Beneficiary's gross estate at the Beneficiary's death under § 2041(a)(2). Further, each Beneficiary will be treated as the transferor of the trust corpus for GST tax purposes under § 2652(a)(1).

Accordingly, the terms of each Further Trust will not extend the time for vesting of any beneficial interest in the trust in a manner that may postpone or suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date the original trust, Trust A, became irrevocable, extending beyond any life in being at the date the original trust became irrevocable plus a period of 21 years. Moreover, each Further Trust will not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the trustee action. Therefore, based on the facts submitted and representations made, we conclude that the merger of Trust A into Trust B will not cause the portion of Trust A merged into Trust B to lose its status as a "grandfathered" trust exempt from GST tax under § 26.2601-1(b). Further, future distributions from Trust B attributable to assets received from Trust A to Son or Beneficiary (as defined in Trust B) will not be subject to GST tax.

### Ruling 2

Section 2652(a)(1) provides that for purposes of chapter 13 the term "transferor" means: (A) in the case of any property subject to the tax imposed by chapter 11, the decedent; and (B) in the case of any property subject to the tax imposed by chapter 12,

the donor. An individual shall be treated as transferring any property with respect to which such individual is the transferor.

Section 2654(b)(1) provides that for purposes of this chapter, the portions of a trust attributable to transfers from different transferors shall be treated as separate trusts.

Section 26.2654-1(a)(2)(i) provides that if there is more than one transferor with respect to a trust, the portions of the trust attributable to the different transferors are treated as separate trusts for purposes of chapter 13. Treatment of a single trust as separate trusts under this paragraph does not permit treatment of those portions as separate trusts for purposes of filing returns and payment of tax or for purposes of computing any other tax imposed under the Code. Also, additions to, and distributions from, such trusts are allocated pro rata among the separate trusts unless otherwise expressly provided in the governing instrument.

Section 26.2654-1(a)(5), *Example 5*, illustrates a situation where A transfers \$100,000 to an irrevocable generation-skipping trust; B simultaneously transfers \$50,000 to the same trust. As of the time of the transfers, the single trust is treated as two trusts for purposes of chapter 13. Because A contributed 2/3 of the value of the initial corpus, 2/3 of the single trust principal is treated as a separate trust created by A. Similarly, because B contributed 1/3 of the value of the initial corpus, 1/3 of the single trust is treated as a separate trust created by B. A or B may allocate their GST exemption under § 2632(a) to the respective separate trusts.

In the instant case, Testator is the transferor of the assets in Trust A for purposes of § 2652(a) and Spouse is the transferor of the assets in Trust B for purposes of § 2652(c). Accordingly, pursuant to § 2654(b)(1), Trust A and Trust B, comprising the merged trusts which portions are attributed to two different transferors, will be treated as separate trusts.

Based on the facts submitted and representations made, we conclude that following the merger of Trust A and Trust B, the portion of the merged trust attributable to the assets received from Trust A and the portion of the trust attributable to the assets contributed to Trust B by Spouse, will be treated as separate trusts for GST tax purposes.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Lorraine E. Gardner  
Senior Counsel, Branch 4  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (1)

cc: